

STATE CORPORATION COMMISSION

AT RICHMOND, JULY 14, 2005

APPLICATION OF

APPALACHIAN POWER COMPANY

CASE NO. PUE-2005-00056

For adjustment to capped electric
rates pursuant to § 56-582 B (vi)
of the Code of Virginia

ORDER FOR NOTICE AND HEARING

On July 1, 2005, Appalachian Power Company ("Appalachian" or "Company") filed with the State Corporation Commission ("Commission") an Application seeking adjustment of its capped electric rates pursuant to § 56-582 B (vi) of the Code of Virginia ("Code") and approval of a methodology by which to make adjustments to its capped rates in the future. Appalachian requests that the Commission direct expedited notice to customers and permit the proposed surcharges to be effective, as interim rates subject to refund, for bills rendered on and after August 1, 2005, or as soon thereafter as possible.

The Company states that § 56-582 B (vi) permits recovery of incremental costs for compliance with state and federal environmental laws and regulations ("environmental costs") and for transmission and distribution system reliability ("reliability costs") after July 1, 2004, and that the cost recovery sought in its Application represents the increment of the Company's environmental and reliability costs above such costs incurred prior to July 1, 2004. The 12-month period ended June 30, 2004, is called the "Base Period" in the Application. Such incremental costs also are identified for two later 12-month periods. The first of such later periods is the 12 months ending June 30, 2005 ("Bridge Period"), and the second of such later periods is the 12 months ending June 30, 2006 ("Projected Period").

2005 JUL 14 3:08

Appalachian asserts that at the time of the filing of the Application, it will have incurred incremental costs during the Bridge Period creating an annual revenue requirement of \$13.5 million and expects to incur incremental costs during the Projected Period that will create an additional \$48.6 million annual revenue requirement. The Company proposes to increase its capped rates during the 12-month period August 1, 2005, through July 31, 2006, in the amount of \$62.1 million, the total revenue requirement for the Bridge Period and Projected Period. The Company proposes to recover this revenue requirement through a 9.18% surcharge factor, called the "E&R Factor," applied to customers' bills during the period August 1, 2005, through July 31, 2006. Appalachian proposes that revenue recovered through the E&R Factor would be "trued-up" for any over-recovery or under-recovery of incremental environmental and reliability costs actually incurred by the Company. An over-recovery would be deducted from, and an under-recovery would be added to, the next E&R Factor approved by the Commission under § 56-582 B (vi).

The Company states that Attachment A to its Application sets forth the E&R Factor that it seeks to implement beginning August 1, 2005, which will increase each customer's bill by an equal percentage. Appalachian asserts that this is in accordance with the Commission's practice of considering rate design issues only in general rate cases. In the event, however, that the Commission considers rate design issues in this case, the Company has prepared an exhibit filed with the Application showing the \$62.1 million revenue requirement allocated among the Company's rate schedules to recognize variations in the demand and energy usage of customers served on those rate schedules.

Next, Appalachian requests approval to continue the revenue requirement methodology proposed in its Application for 12-month Projected Periods beginning after June 30, 2006, in

order to determine incremental environmental and reliability costs for purposes of future Applications under § 56-582 B (vi). The Company contends that such methodology is appropriate to maintain timely recovery of such costs as required by the statute, and that with appropriate adjustments for over- or under-recoveries, the proposed methodology accomplishes the statutory direction for timely recovery while protecting customers from over-recovery of such costs.

The Company further asserts that the significant amounts and upward trend of these costs are just beginning and require that recovery of such costs through rates commence as soon as possible. For example, Appalachian states that incremental environmental compliance costs alone in the Projected Period ending July 1, 2006, are expected to create an additional revenue requirement of at least \$31 million, which is more than double the \$13.5 million revenue requirement created by incremental costs for both environmental compliance and transmission and distribution reliability in the immediately preceding Bridge Period ending June 30, 2005.

In addition, the Company requests that in the event the Commission determines to make effective only a portion of its revenue request prior to consideration on the merits, such portion should be made effective for bills rendered on and after August 1, 2005, or as soon thereafter as possible. Appalachian states that to the extent costs whose recovery is authorized by § 56-582 B (vi) are not recovered on a current basis under the E&R Factor as the Commission may authorize, the Company would defer such unrecovered costs. Then, when the Commission has completed its consideration of the Application and to the extent the Commission determines that such costs are eligible for recovery under § 56-582 B (vi), the Company in its next Application would seek their recovery beginning immediately after the end of the E&R Factor authorized by the Commission in this proceeding.

NOW UPON CONSIDERATION of the Application and applicable law, the Commission is of the opinion and finds as follows. This matter shall be docketed, a procedural schedule shall be established, and Appalachian shall give notice of its Application, all as prescribed below.

In addition, the Company shall not implement any portion of the Application until further order of the Commission. Specifically, Appalachian requests the Commission to permit the proposed surcharges to become effective, as interim rates subject to refund, for bills rendered on and after August 1, 2005, or as soon as possible thereafter. The Company also addresses the possibility that the Commission may make effective only a portion of the revenue request prior to consideration on the merits. However, § 56-582 B (vi) of the Code does not state that the Commission has the authority to make any portion of the Company's proposed surcharges interim and subject to refund. Thus, we shall establish a date for legal memoranda on this question and thereafter issue an order during the pendency of this proceeding on Appalachian's request for interim rates subject to refund.¹

Accordingly, IT IS ORDERED THAT:

(1) The Company's Application is hereby docketed and assigned Case No.

PUE-2005-00056.

(2) No portion of the Application shall become effective pending further order of the Commission.

(3) A copy of the Application and this Order for Notice and Hearing, as well as other documents now or hereafter filed in this matter, shall be available for public inspection in the Commission's Document Control Center located on the First Floor of the Tyler Building,

¹ Such preliminary briefing schedule does not preclude other legal issues from being raised during this proceeding.

1300 East Main Street, Richmond, Virginia, between the hours of 8:15 a.m. and 5:00 p.m., Monday through Friday. A copy of the Application also may be obtained by requesting a copy of the same from counsel for Appalachian, Anthony Gambardella, Esquire, Woods Rogers PLC, 823 East Main Street, Suite 1200, Richmond, Virginia 23219. Upon receipt of a request for a copy of the Application, the Company shall serve copies of the same upon the requesting party within three (3) business days of such request. If acceptable to the requesting party, the Company may provide the Application, with or without attachments, by electronic means. In addition, the Commission's Order For Notice and Hearing and other orders entered in these dockets, the Commission's Rules of Practice and Procedure, as well as other information concerning the Commission and the statutes it administers, may be viewed on the Commission's website at <http://www.scc.virginia.gov>.

(4) A public hearing shall be convened on February 7, 2006, at 10:00 a.m., in the Commission's Courtroom, Second Floor, Tyler Building, 1300 East Main Street, Richmond, Virginia, to receive comments from members of the public and to receive evidence in the above-captioned docket. Any person not participating as a respondent as provided for below may give oral testimony concerning this case as a public witness at the hearing. Public witnesses desiring to make statements at the public hearing need only appear in the Commission's Second Floor courtroom in the Tyler Building at the address set forth above prior to 9:45 a.m. on the day of the hearing and register a request to speak with the Commission's bailiff.

(5) On or before August 15, 2005, the Company shall file with the Clerk, State Corporation Commission, c/o Document Control Center, P.O. Box 2118, Richmond, Virginia, 23218-2118, an original and fifteen (15) copies of any additional direct testimony, exhibits and other material supporting its Application.

(6) Any interested person may participate as a respondent in this proceeding by filing, on or before September 6, 2005, an original and fifteen (15) copies of a notice of participation with the Clerk at the address in Ordering Paragraph (10), and shall simultaneously serve a copy of the notice of participation on counsel to Appalachian at the address in Ordering Paragraph (3). Pursuant to Rule 5 VAC 5-20-80 of the Commission's Rules of Practice and Procedure, any notice of participation shall set forth: (i) a precise statement of the interest of the respondent; (ii) a statement of the specific action sought to the extent then known; and (iii) the factual and legal basis for the action. Interested parties shall refer in all of their filed papers to Case No. PUE-2005-00056.

(7) Within five (5) business days of receipt of a notice of participation as a respondent, the Company shall serve upon each respondent a copy of this Order for Notice and Hearing, a copy of the Application, and all materials filed by the Company with the Commission, unless these materials have already been provided to the respondent.

(8) On or before September 6, 2005, the Company, each respondent, and the Commission Staff may file legal memoranda on whether, and under what circumstances, the Commission has the authority to make effective, on an interim basis subject to refund, any portion of the rates proposed in the Application.

(9) On or before November 29, 2005, each respondent may file with the Clerk an original and fifteen (15) copies of any testimony and exhibits by which it expects to establish its case and shall serve copies of the testimony and exhibits on counsel to the Company and on all other respondents. The respondent shall comply with the Commission's Rules of Practice and Procedure, including: 5 VAC 5-20-140, *Filing and service*; 5 VAC 5-20-150, *Copies and format*; and 5 VAC 5-20-240, *Prepared testimony and exhibits*.

(10) On or before November 29, 2005, any interested person may file with the Clerk, State Corporation Commission, c/o Document Control Center, P.O. Box 2118, Richmond, Virginia 23218-2118, written comments on the Application and shall simultaneously serve a copy on counsel to Appalachian at the address in Ordering Paragraph (3). On or before November 29, 2005, any interested person desiring to submit comments electronically may do so by following the instructions found on the Commission's website: <http://www.scc.virginia.gov/caseinfo.htm>.

(11) The Commission Staff shall investigate the Application. On or before January 10, 2006, the Staff shall file with the Clerk of the Commission an original and fifteen (15) copies of the Staff's testimony and exhibits and shall serve a copy on counsel to the Company and all respondents.

(12) On or before January 26, 2006, Appalachian shall file with the Clerk of the Commission an original and fifteen (15) copies of any rebuttal testimony and exhibits and shall serve a copy on the Staff and all respondents.

(13) On or before August 8, 2005, Appalachian shall cause the following notice to be published as display advertising (not classified) in newspapers of general circulation throughout the Company's service territory within the Commonwealth of Virginia in the following form:

NOTICE TO THE PUBLIC OF
APPALACHIAN POWER COMPANY'S
APPLICATION FOR ADJUSTMENT
TO CAPPED ELECTRIC RATES
CASE NO. PUE-2005-00056

On July 1, 2005, Appalachian Power Company ("Appalachian" or "Company") filed with the State Corporation Commission ("Commission") an Application seeking adjustment of its capped electric rates pursuant to § 56-582 B (vi) of the Code of Virginia ("Code") and approval of a methodology by which to make adjustments to its capped rates in the future. Appalachian requests that the Commission direct expedited notice to customers and permit the proposed surcharges to be effective, as interim rates

subject to refund, for bills rendered on and after August 1, 2005, or as soon thereafter as possible.

The Company states that § 56-582 B (vi) permits recovery of incremental costs for compliance with state and federal environmental laws and regulations ("environmental costs") and for transmission and distribution system reliability ("reliability costs") after July 1, 2004, and that the cost recovery sought in its Application represents the increment of the Company's environmental and reliability costs above such costs incurred prior to July 1, 2004. The 12-month period ended June 30, 2004 is called the "Base Period" in the Application. Such incremental costs also are identified for two later 12-month periods. The first of such later periods is the 12 months ending June 30, 2005 ("Bridge Period"), and the second of such later periods is the 12 months ending June 30, 2006 ("Projected Period").

Appalachian asserts that at the time of the filing of the Application, it will have incurred incremental costs during the Bridge Period creating an annual revenue requirement of \$13.5 million and expects to incur incremental costs during the Projected Period that will create an additional \$48.6 million annual revenue requirement. The Company proposes to increase its capped rates during the 12-month period August 1, 2005, through July 31, 2006, in the amount of \$62.1 million, the total revenue requirement for the Bridge Period and Projected Period. The Company proposes to recover this revenue requirement through a 9.18% surcharge factor, called the "E&R Factor," applied to customers' bills during the period August 1, 2005, through July 31, 2006. Appalachian proposes that revenue recovered through the E&R Factor would be "trued-up" for any over-recovery or under-recovery of incremental environmental and reliability costs actually incurred by the Company. An over-recovery would be deducted from, and an under-recovery would be added to, the next E&R Factor approved by the Commission under § 56-582 B (vi).

The Company states that Attachment A to its Application sets forth the E&R Factor that it seeks to implement beginning August 1, 2005, which will increase each customer's bill by an equal percentage. In the event, however, that the Commission considers rate design issues in this case, the Company has prepared an exhibit filed with the Application showing the \$62.1 million revenue requirement allocated among the Company's rate schedules to recognize variations in the demand and energy usage of customers served on those rate schedules. Appalachian requests approval to continue the revenue requirement methodology

proposed in its Application for 12-month Projected Periods beginning after June 30, 2006, in order to determine incremental environmental and reliability costs for purposes of future Applications under § 56-582 B (vi).

The Company further asserts that the significant amounts and upward trend of these costs are just beginning and require that recovery of such costs through rates commence as soon as possible. For example, Appalachian states that incremental environmental compliance costs alone in the Projected Period ending July 1, 2006, are expected to create an additional revenue requirement of at least \$31 million, which is more than double the \$13.5 million revenue requirement created by incremental costs for both environmental compliance and transmission and distribution reliability in the immediately preceding Bridge Period ending June 30, 2005.

In addition, the Company requests that in the event the Commission determines to make effective only a portion of its revenue request prior to consideration on the merits, such portion should be made effective for bills rendered on and after August 1, 2005, or as soon thereafter as possible. Appalachian states that to the extent costs whose recovery is authorized by § 56-582 B (vi) are not recovered on a current basis under the E&R Factor as the Commission may authorize, the Company would defer such unrecovered costs. Then, when the Commission has completed its consideration of the Application and to the extent the Commission determines that such costs are eligible for recovery under § 56-582 B (vi), the Company in its next Application would seek their recovery beginning immediately after the end of the E&R Factor authorized by the Commission in this proceeding.

The Company's Application is docketed and assigned Case No. PUE-2005-00056. No portion of the Application shall become effective pending further order of the Commission. Interested persons are encouraged to review the Application and the Commission's Order for Notice and Hearing. Interested persons should be advised that, after considering all of the evidence, the Commission may approve, reject, or modify the Application, may approve revenues and adopt rates, fees, charges, methodologies, and terms and conditions of service that are the same or different from those appearing in the Application, and/or may apportion revenues among customer classes in a manner that is the same or different from that in the Application.

Interested persons may review a copy of the Application and the Commission's Order for Notice and Hearing in the Commission's Document Control Center, located on the First Floor of the Tyler Building, 1300 East Main Street, Richmond, Virginia between the hours of 8:15 a.m. and 5:00 p.m., Monday through Friday. A copy of the Application may also be obtained at no cost by interested persons by making a written request to the Company's counsel, Anthony Gambardella, Esquire, Woods Rogers PLC, 823 East Main Street, Suite 1200, Richmond, Virginia 23219. If acceptable to the requesting party, the Company may provide the Application, with or without attachments, by electronic means. In addition, the Commission's Order For Notice and Hearing and other orders entered in this docket, the Commission's Rules of Practice and Procedure, as well as other information concerning the Commission and the statutes it administers, may be viewed on the Commission's website at <http://www.scc.virginia.gov>.

A public hearing shall be convened on February 7, 2006, at 10:00 a.m., in the Commission's Courtroom, Second Floor, Tyler Building, 1300 East Main Street, Richmond, Virginia, to receive comments from members of the public and to receive evidence in both of the above-referenced dockets. Any person not participating as a respondent as provided for below may give oral testimony concerning this case as a public witness at the hearing. Public witnesses desiring to make statements at the public hearing need only appear in the Commission's Second Floor courtroom in the Tyler Building at the address set forth above prior to 9:45 a.m. on the day of the hearing and register a request to speak with the Commission's bailiff.

Any interested person may participate as a respondent in this proceeding by filing, on or before September 6, 2005, an original and fifteen (15) copies of a notice of participation with the Clerk, State Corporation Commission, c/o Document Control Center, P.O. Box 2118, Richmond, Virginia 23218-2118, and shall simultaneously serve a copy of the notice of participation on counsel to Appalachian at the address above. Pursuant to Rule 5 VAC 5-20-80 of the Commission's Rules of Practice and Procedure, any notice of participation shall set forth: (i) a precise statement of the interest of the respondent; (ii) a statement of the specific action sought to the extent then known; and (iii) the factual and legal basis for the action. Interested parties shall refer in all of their filed papers to Case No. PUE-2005-00056.

On or before September 6, 2005, the Company, each respondent, and the Commission Staff may file legal memoranda on whether, and under what circumstances, the Commission has the authority to make effective, on an interim basis subject to refund, any portion of the rates proposed in the Application.

On or before November 29, 2005, any interested person may file with the Clerk of the Commission, at the address set forth above, written comments on the Application and shall simultaneously serve a copy on counsel to Appalachian at the address above. On or before November 29, 2005, any interested person desiring to submit comments electronically may do so by following the instructions found on the Commission's website: <http://www.scc.virginia.gov/caseinfo.htm>.

On or before November 29, 2005, each respondent may file with the Clerk of the Commission at the address above an original and fifteen (15) copies of any testimony and exhibits by which it expects to establish its case and shall serve copies of the testimony and exhibits on counsel to the Company at the address above and on all other respondents. The respondent shall comply with the Commission's Rules of Practice and Procedure, including: 5 VAC 5-20-140, *Filing and service*; 5 VAC 5-20-150, *Copies and format*; and 5 VAC 5-20-240, *Prepared testimony and exhibits*.

APPALACHIAN POWER COMPANY

(14) On or before August 8, 2005, Appalachian shall forthwith serve a copy of its Application and this Order for Notice and Hearing on the Chairman of the Board of Supervisors and county attorney of each county and on the Mayor or Manager of every city and town (or on equivalent officials in counties, towns, and cities having alternate forms of government) in which Appalachian provides service. Service shall be made by personal delivery or by first-class mail, postage prepaid, to the customary place of business or residence of the person served.

(15) On or before September 6, 2005, Appalachian shall file with the Clerk of the Commission proof of the notice required in Ordering Paragraphs (13) and (14).

(16) The Commission's Rules of Practice and Procedure, 5 VAC 5-20-260, *Interrogatories to parties or requests for production of documents and things*, shall be modified

for this proceeding as follows: (i) answers shall be served within ten (10) calendar days after receipt of interrogatories or requests for production of documents; (ii) objections shall be served within seven (7) calendar days after receipt of interrogatories or requests for production of documents; and (iii) motions on the validity of any objections shall be filed within ten (10) calendar days of receipt of any objection.

(17) As provided by § 12.1-31 of the Code of Virginia and the Commission's Rules of Practice and Procedure, 5 VAC 5-20-120, *Procedure before hearing examiners*, a hearing examiner is appointed to conduct further proceedings in this matter on behalf of the Commission and to issue a final report herein.

(18) This matter is continued pending further order of the Commission.

AN ATTESTED COPY hereof shall be sent by the Clerk of the Commission to:
Anthony Gambardella, Esquire, Woods Rogers P.L.C., 823 East Main Street, Suite 1200,
Richmond, Virginia 23219; C. Meade Browder, Jr., Senior Assistant Attorney General, Division
of Consumer Counsel, Office of Attorney General, 900 East Main Street, 2nd Floor, Richmond,
Virginia 23219; and the Commission's Office of General Counsel and Division of Energy
Regulation, Public Utility Accounting, and Economics and Finance.